

Message Text

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ACTION EUR-25

INFO OCT-01 EA-11 ISO-00 CIAE-00 COME-00 EB-11 INR-10

LAB-06 NSAE-00 RSC-01 SIL-01 FRB-02 DODE-00 PM-07

H-03 L-03 NSC-10 PA-03 PRS-01 SPC-03 SS-15 USIA-15

ACDA-19 IO-15 STR-08 OMB-01 CEA-02 CIEP-02 DRC-01

TAR-02 XMB-07 AGR-20 /205 W
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R 101632Z OCT 73

FM AMEMBASSY LONDON
TO SECSTATE WASHDC 4636
INFO AMEMBASSY BONN
AMEMBASSY BRUSSELS
AMEMBASSY COPENHAGEN
AMEMBASSY DUBLIN
AMEMBASSY PARIS
AMEMBASSY ROME
AMEMBASSY THE HAGUE
AMEMBASSY TOKYO
USMISSION EC BRUSSELS
USMISSION OECD PARIS
TREASURY DEPT WASHDC

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DEPARTMENT ALSO PASS DEPT OF LABOR AND FRB

E.O. 11652: N/A

TAGS: ECON, UK

SUBJECT: STAGE THREE OF U.K. WAGE-PRICE PROGRAM

REF: LONDON 3843

BEGIN SUMMARY: GOVERNMENT ISSUED CONSULTATIVE DOCUMENT
ON OCTOBER 8 DETAILING PROPOSALS FOR STAGE THREE OF
PRICE-WAGE PROGRAM. BASIC STRUCTURE OF STAGE TWO CODE
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REMAINS BUT PARAMETERS ARE MORE LIBERAL AND ADD FLEXIBI-

LITY. NEW WRINKLES INCLUDE TEN PERCENT LIMIT ON PROFIT REDUCTIONS WHICH RESULT FROM NOT BEING ABLE TO RAISE PRICES TO FULLY COVER COSTS, REQUIREMENT THAT MIDDLE SIZED FIRMS REPORT PRICE RISES IMMEDIATELY, POWER OF PRICE COMMISSION TO SET PRICE STANDARDS FOR WHOLE SECTORS OF INDUSTRIES, AND ON THE WAGE SIDE, THRESHOLD ARRANGEMENTS. PENSIONERS AND HOMEOWNERS PROMISED AID. DIVIDEND LIMIT OF FIVE PERCENT INCREASE OVER PREVIOUS YEAR OF STAGE TWO REMAINS. IMPACT OF PROGRAM ON DEMAND BELIEVED BY GOVERNMENT TO BE NEUTRAL. THE KEYS TO THE SUCCESS OF STAGE THREE APPEAR TO BE LIMITING PUBLIC EXPENDITURE AND A SLOWDOWN OR REVERSE OF IMPORT PRICE RISES. GOVERNMENT HAS INFORMALLY CONSULTED WITH BUSINESS AND LABOR PRIOR TO PROGRAM'S PUBLICATION, BUT WILL NOW FORMALLY CONSULT WITH ALL INTERESTED PARTIES UNTIL IT SEEKS TO IMPLEMENT PROGRAM (NOVEMBER 1 FOR PRICES, NOVEMBER 7 FOR WAGES). END SUMMARY.

1. NEW LIMITS ON WAGE INCREASES ARE SEVEN PERCENT OF AVERAGE PER WORKER WAGE BILL OF GROUP OVER PRECEDING YEAR OR FLAT 2.25 POUNDS PER WEEK PER INDIVIDUAL. LATTER ALTERNATIVE AIMED AT RELATIVE IMPROVEMENT OF LOWER PAID WORKERS. THE OUTER LIMIT PER INDIVIDUAL IS 350 POUNDS PER YEAR.

2. TO BROADEN SCOPE FOR WAGE NEGOTIATIONS, HELP ELIMINATE "ANOMALIES", PROVIDE FOR SOME FLEXIBILITY AND ALLEVIATE MANPOWER SHORTAGES IN SOME SECTORS (LONDON TRANSPORT IS OPERATING AT ABOUT 80-85 PERCENT OF PITIUM STAFF), PROGRAM HAS FOLLOWING PROVISIONS:
A. WAGE LIMIT MAY BE EXTENDED BY ONE PERCENT TO "REMEDY ANOMALIES" OR "IMPROVE EFFICIENCY." THIS MAY INCLUDE IMPROVEMENT OF SICK OR VACATION BENEFITS.

B. SPECIAL SCHEMES TO INCREASE PRODUCTIVITY ARE NOT SUBJECT TO THE LIMIT. THESE SCHEMES MUST, HOWEVER, HAVE PRIOR APPROVAL OF THE PAY BOARD WHICH MUST HAVE THREE MONTHS EVIDENCE OF SCHEME'S EFFICACY.

C. PREMIUM PAYMENTS FOR THOSE WORKING "UNSOCIAL HOURS" I.E., NIGHTS AND/OR WEEKENDS, NOT SUBJECT TO UNCLASSIFIED

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LIMITS.

D. ALLOWANCES FOR EXTRA EXPENSE OF WORKING IN LONDON NOT SUBJECT TO LIMITS, PROVIDED SUCH ALLOWANCE IN EXISTENCE PRIOR TO NOVEMBER 1972.

3. DESPITE OBJECTIONS OF BOTH TUC AND CBI, GOVERNMENT PROGRAM INCLUDES A THRESHOLD ARRANGEMENT. BASE IS RETAIL PRICE INDEX OF OCTOBER 1973. IF INDEX INCREASES

BY SEVEN PERCENT IN SUBSEQUENT 12 MONTH PERIOD, WAGES MAY BE INCREASED BY 40 PENCE PER WEEK (ABOUT 97 CENTS). FOR EACH PERCENTAGE POINT INCREASE BEYOND THAT, DURING THE 12 MONTH PERIOD, WAGES MAY BE INCREASED BY ANOTHER 40 PENCE.

4. PROGRAM ALLOWS "SHARE SAVINGS SCHEMES," AUTHORIZED IN FINANCE ACT OF 1973 TO OPERATE WHILE OTHER SHARE OPTION AND SHARE INCENTIVE SCHEMES REMAIN SUBJECT TO RESTRICTIONS OF STAGE TWO. THESE "SHARE SAVINGS SCHEMES" PERMIT WORKERS TO PURCHASE EQUITIES OF EMPLOYING FIRMS ON PAY-AS-YOU-DO BASIS AT ADVANTAGEOUS PRICES.

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TAR-02 XMB-07 AGR-20 /205 W
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R 101632Z OCT 73

FM AMEMBASSY LONDON
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INFO AMEMBASSY BONN
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5. GOVERNMENT ALSO PROPOSES THAT JANUARY 1
BE MADE A BANK HOLIDAY.

6. ON PRICE SIDE, MORE FLEXIBILITY INTRODUCED BUT THERE
WILL ALSO BE STRICTER CONTROL, ESPECIALLY OF SMALLER
UNITS. MAIN FEATURES OF STAGE TWO WILL REMAIN IN
FORCE. THIS INCLUDES LIMIT ON PRICE RISES TO "ALLOWABLE
COSTS," WITH A DEDUCTION OF UP TO 50 PERCENT FOR
PRODUCTIVITY. ALLOWABLE COSTS DEFINITION HAS BEEN
BROADENED TO INCLUDE INTER ALIA DEPRECIATION (CALCULATED
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ON GENERALLY ACCEPTED PRINCIPLES).

7. PROFIT MARGIN LIMITS OF STAGE TWO WILL CONTINUE.
ARTIFICIAL SUBDIVISION OF FIRMS TO GAIN EDGE
ON PROFIT LIMITS WILL BE DISCONTINUED. HOWEVER, TO
HELP ENHANCE INVESTMENT THERE ARE SEVERAL NEW FEATURES.
WHERE ALLOWABLE COST PROVISIONS OR PRODUCTIVITY DEDUC-
TION WOULD REDUCE PROFITS FROM BASE PERIOD MORE THAN
10 PERCENT, THE REDUCTION MAY BE LIMITED TO 10 PERCENT.
ALSO COMPANIES EARNING LESS THAN 8 PERCENT RETURN ON
CAPITAL MAY INCREASE PRICES UNTIL THAT RETURN ATTAINED
WITHOUT REFERENCE TO LIMITATIONS OF CODE. THERE ARE
ALSO SPECIAL ARRANGEMENTS FOR NEW FIRMS WHICH MAY HAVE
PRODUCED AT LOW PERCENTAGE OF CAPACITY IN PREVIOUS
PERIOD.

INCREASES AS THEY ARE MADE. UNDER STAGE TWO THEY REPOR-
TED QUARTERLY. ALSO UNDER THE PROPOSED PROGRAM THE
PRICE COMMISSION WILL HAVE THE POWER TO ROLL BACK PRICES
IN A WHOLE SECTOR OF AN INDUSTRY.

9. NATIONALIZED INDUSTRIES MUST LIMIT PRICE RISES
STRICTLY WITHIN CODE LIMITS. DEFICITS WILL BE FINANCED
BY GOVERNMENT.

10. BANKS WILL NOT RECEIVE INTEREST ON
PROPORTION OF SPECIAL DEPOSITS.

11. GOVERNMENT WILL SPREAD OUT PUBLIC PROJECTS TO
MITIGATE CONSTRUCTION PRICE RISES.

12. DIVIDEND CONTROL OF NOT MORE THAN FIVE PERCENT
INCREASE FROM PREVIOUS YEAR WILL REMAIN IN EFFECT.

13. REACTION. AS COULD BE EXPECTED, BOTH SIDES OF INDUSTRY AS WELL AS LABOR PARTY WERE CRITICAL OF PROGRAM. CBI BELIEVES WAGE LIMITS TOO LIBERAL AND "POSSIBLY MORE EXPENSIVE THAN ECONOMY CAN STAND." THEY CALCULATE CONSUMPTION CANNOT INCREASE BY MORE THAN 2-1/2 PERCENT. GOVERNMENT PROGRAM WOULD IMPLY A UNCLASSIFIED

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HIGHER INCREASE. CBI ALSO BELIEVES THRESHHOLD PROVISIONS TRIGGERED AT TOO LOW A LEVEL AND UPPER LIMIT ON INDIVIDUAL WAGE INCREASES TOO RESTRICTIVE.

14. INITIAL REACTION BY TUC WAS COOL BUT MIXED. DETAILS IN TELEGRAM TO FOLLOW.

15. ANTHONY HARRIS IN FINANCIAL TIMES STATES GOVERNMENT IS GAMBLING ON LEVELING OFF OR DECREASE IN IMPORT COSTS. IF SUCH COSTS DO FALL, HARRIS BELIEVES FIRMS WILL HAVE INCENTIVE TO ABSORB DOMESTIC COSTS INCREASES WITH A REALISTIC HOPE OF HIGHER PROFITS GIVEN 10 PERCENT LIMIT ON PROFIT REDUCTIONS. IF EXTERNAL COSTS CONTINUE TO RISE, HOWEVER, THIS LIMITATION ON PROFIT REDUCTIONS MEANS THAT CONTROLS WILL HAVE LITTLE EFFECT. IN EFFECT, HARRIS SAYS THAT THIS 10 PERCENT LIMIT COULD TURN CODE INTO "COST-PLUS FORMULA," IF EXTERNAL COSTS RISE. HARRIS ALSO POINTS OUT THAT INCLUSION OF DEPRECIATION IN ALLOWABLE COSTS IS MEANINGFUL INVESTMENT INCENTIVE IN THAT COMPANIES MUST INCLUDE IT. THOSE WHICH HAVE NOT BEEN INVESTING MAY NOT BE ABLE TO JUSTIFY AS LARGE PRICE INCREASES AS UNDER STAGE TWO.

16. COMMENT. OUTLOOK FOR SUCCESS OF STAGE THREE IN CONTINUING TO MITIGATE INFLATIONARY TENDENCIES IN UK ECONOMY IS HIGHLY TENTATIVE. GOVERNMENT CLAIMS THAT THE PROGRAM'S EFFECT ON DEMAND WILL BE NEUTRAL BUT MANY OBSERVERS ARE SKEPTICAL. ALL SEEM TO AGREE THAT TOTAL OUTPUT CAN NOT GROW AT MORE THAN 3-1/2 PERCENT IN 1974. (THE GROWTH LIMIT OF CAPACITY) AND CONSUMPTION, INVESTMENT, AND EXPORTS MUST SHARE

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THIS. INVESTMENT PLANS REPORTED HIGH BY RECENT FINANCIAL
TIMES SURVEY. DESPITE WAGE LIMITS, TOTAL EARNINGS
LIKELY TO RISE BY ABOUT ELEVEN PERCENT WHICH COULD FUEL
CONSUMER DEMAND AND REVERSE ITS RECENT LEVELLING OFF
TREND. THUS PROSPECT COULD BE THAT EXPORTS WOULD
SUFFER WHICH WOULD IMPAIR ANTI-INFLATIONARY MONETARY
POLICY OR INCREASE IMPORT PRICES THROUGH STERLING
DEPRECIATION.

17. EFFECTIVENESS OF MORE LIBERAL PRICE POLICIES
(ESPECIALLY PROFIT MARGINS) DEPENDENT ON EXTERNAL
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COSTS AND ON ATTITUDE OF MANAGEMENT. WITH COST DECREASES
AND DOMESTIC DEMAND FALL THEY STILL MUST BE WILLING TO
ABSORB DOMESTIC COSTS (PRICE MOVEMENTS HAVE BEEN

LIMITED ON MANY SINCE VOLUNTARY CBI PRICE
PROGRAM OF 1971) AND TAKE ADVANTAGE OF INVESTMENT AND
EXPORT OPPORTUNITIES.

18. HOLDING NATIONALIZED INDUSTRY TO PRICE LIMITS
PRESENTS ANOTHER DANGER AS GOVERNMENT COMMITTED NOW
TO FINANCING DEFICITS. IF THIS INCREASES GOVERNMENT
DEFICIT AND BORROWING REQUIREMENT, INFLATIONARY TENDEN-
CIES COULD BE EXACERBATED. HOWEVER, PUBLIC EXPENDITURE
PREDICTED TO GROW MUCH MORE SLOWLY, AND SPREADING OUT
PUBLIC CONSTRUCTION WILL HELP ON THIS SCORE.

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Message Attributes

Automatic Decaptioning: X
Capture Date: 01 JAN 1994
Channel Indicators: n/a
Current Classification: UNCLASSIFIED
Concepts: WAGES, COST OF LIVING, PRICE CONTROLS, WAGE PRICE INDEXES, ANTIINFLATIONARY PROGRAMS
Control Number: n/a
Copy: SINGLE
Draft Date: 10 OCT 1973
Decaption Date: 01 JAN 1960
Decaption Note:
Disposition Action: n/a
Disposition Approved on Date:
Disposition Authority: n/a
Disposition Case Number: n/a
Disposition Comment:
Disposition Date: 01 JAN 1960
Disposition Event:
Disposition History: n/a
Disposition Reason:
Disposition Remarks:
Document Number: 1973LONDON11682
Document Source: CORE
Document Unique ID: 00
Drafter: n/a
Enclosure: n/a
Executive Order: N/A
Errors: N/A
Film Number: n/a
From: LONDON
Handling Restrictions: n/a
Image Path:
ISecure: 1
Legacy Key: link1973/newtext/t19731041/aaaabedx.tel
Line Count: 344
Locator: TEXT ON-LINE
Office: ACTION EUR
Original Classification: UNCLASSIFIED
Original Handling Restrictions: n/a
Original Previous Classification: n/a
Original Previous Handling Restrictions: n/a
Page Count: 7
Previous Channel Indicators:
Previous Classification: n/a
Previous Handling Restrictions: n/a
Reference: LONDON 3843
Review Action: RELEASED, APPROVED
Review Authority: hilburpw
Review Comment: n/a
Review Content Flags:
Review Date: 08 AUG 2001
Review Event:
Review Exemptions: n/a
Review History: RELEASED <08-Aug-2001 by reddocgw>; APPROVED <16-Aug-2001 by hilburpw>
Review Markings:

Declassified/Released
US Department of State
EO Systematic Review
30 JUN 2005

Review Media Identifier:
Review Referrals: n/a
Review Release Date: n/a
Review Release Event: n/a
Review Transfer Date:
Review Withdrawn Fields: n/a
Secure: OPEN
Status: NATIVE
Subject: STAGE THREE OF U.K. WAGE-PRICE PROGRAM
TAGS: ECON, UK
To: STATE
Type: TE
Markings: Declassified/Released US Department of State EO Systematic Review 30 JUN 2005